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SUBJECT: Government Enacts Controversial Tax Laws to Streamline and Lower Rates, and Empower Tax Authorities

Refs: A) 09 Amman 2673

- B) 09 Amman 2572
- C) 09 Amman 2562
- D) 08 Amman 1834

¶1. (SBU) Summary: The Government of Jordan enacted recently two new tax laws to lower income tax rates and grant greater powers to tax authorities. The laws, which will remain in force until a new parliament is elected and votes on them, represent the first notable achievement of the new government and were well received by the business community and individuals. As of January 1, 2010, under the Temporary Income Tax Law, families with incomes less than \$34,000 are exempt from taxes. Corporate income taxes, as well as taxes for telecommunications companies, financial service providers, and banks were also lowered. The Temporary General Sales Tax Law deals with administrative matters, the collection mechanism, and the appeals process. The new laws also provide more power and authority to the Director of the Tax Department, but with tax evasion not considered a felony, the penalties remain an insufficient deterrent. The positive effects of the new laws, however, will not be seen before 2011. The first year of this new tax program was intended to be revenue neutral, but due to a difficult budgetary situation, the GOJ anticipates that tax revenues will actually decline in 2010, which it hopes to offset by collecting increased sales taxes. USG technical assistance was critical to these important changes to the tax structure. End summary.

Tax Reform to Reduce Poverty and Attract Investment

¶2. (SBU) Under instructions from the King, successive Jordanian governments have worked on tax reform for almost five years with the goals of encouraging investment, alleviating poverty, and eliminating tax disparities by simplifying the tax code, increasing tax collection efficiency, and curbing evasion. Upon publication in the Official Gazette on December 30, 2009, the GOJ enacted two temporary laws that achieve some of these goals. The combined statutes of the new Temporary Income Tax Law and new Temporary General Sales Tax Law, legislation that had been viewed as controversial and contributed to the stand-off and ultimate dismissal of the former cabinet and parliament, rationalize

individual income tax rates, simplify the tax structure for many lower and middle income families, eliminate loopholes used by individuals and businesses to reduce or avoid their tax burdens, cancel a number of indirect taxes, and give new authorities to the Tax Department and the cabinet (ref C).

13. (SBU) Musa Mawazreh, Director General of the Tax Department, is proud of the changes and told EconSpec the new laws were a top priority for the new government, commenting that officials worked around-the-clock for two weeks to complete the legislation. Mawazreh speculated the temporary laws, because the GOJ incorporated several of the changes desired by the previous parliament, would pass through the next parliament smoothly and become permanent. (Note: Temporary laws are passed when parliament is dissolved or not in session. Once a new parliament is in place, temporary laws must be presented for approval, but they remain in force until parliament takes action (ref D). End note.) Much of the private sector also praised the changes. Imad Marar, CEO of the National Bank of Abu Dhabi, scheduled to open soon in Jordan, welcomed the changes on both a professional and personal level. He described the new laws as simple and just, explaining they narrowed the gaps between different tax payers and sectors.

#### Lower, but Standardized Rates Across the Board

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14. (U) Both individuals and companies will benefit from the legislative changes. According to the new Income Tax Law, the first \$17,000 of an individual's income and the first \$34,000 of a family's income are tax free. Additional income is taxed at 7% for

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the next \$17,000 and 14% thereafter. This is a much simpler, clearer, and fairer formula that eliminates exemptions that taxpayers previously could claim for spouses, children, parental support, rent and mortgages, educational expenses, universities, and healthcare. Corporate income tax has been reduced to 14%, down from the 15% or 25% previously paid depending on the type of company. Telecommunications and financial service providers are now taxed at 24%, and banks at 30% instead of 25% and 35%, respectively. While the law eliminates many exemptions, the cabinet gained the right to grant them on a case-by-case basis.

#### Welcomed Changes Amid Compromises

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15. (SBU) The GOJ made some compromises and incorporated several of the previous parliament's recommended suggestions. The government's initial draft laws proposed that corporate income for all sectors be taxed at 12% and banks at 25%. The previous parliament refused, a decision that, in hindsight, was beneficial to the GOJ given the current budget situation (ref A). The former parliament also refused to tax the agricultural sector. The new law treats most farmers as individuals, exempting a good portion of their income, and after an exemption on the first \$75,000 of income, taxes agricultural companies at the 14% corporate rate. Another compromise that the GOJ accepted relates to pension income and end-of-service indemnities. The government opted to temporarily exempt, in addition to the \$17,000 or \$34,000 of tax-free income, taxes on the first \$5,600 of pension income as well as on 50% of end-of-service benefits. Mawazreh elaborated that within two years, the GOJ anticipates amending the relevant articles to remove most such exemptions. He added this approach was used by previous governments for similar controversial matters and proved successful in obtaining public support.

#### Majority of Indirect Taxes Cancelled

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16. (SBU) The new laws repeal numerous previous laws that imposed approximately 100 different kinds of taxes, which, in effect, hindered Jordan's efforts to compete for foreign direct investment. The new laws strive to reverse this situation and annul a range of taxes, including those on the value of imported products, properties, income tax, and livestock used for social purposes as well as indirect taxes to compensate tribal sheikhs and military

army personnel and to combat diseases such as HIV, malaria, and tuberculosis. Also repealed were the youth tax, cultural tax, municipality tax, and handicapped tax which supported these social sectors.

#### More Power to Cabinet and Tax Department

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17. (U) The new Income Tax Law provides the cabinet with the authority to reduce gradually taxes by one percent each year to reach targeted rates of 5% (down from 7%) for lower income individuals and 10% (from 14%) for the higher income bracket. There are also targets to eventually halve corporate income tax to 10% and reduce to 20% the tax for telecommunications companies, and financial service providers and banks, down from 24% and 30% respectively. Additionally, the Income Tax Law provides considerable power to the Director General of the Tax Department and his staff. The Director General, with the Finance Minister's approval, can prevent tax scofflaws from traveling, even without a court ruling. He also has the power to confiscate property and funds if amounts due to the Tax Department exceed \$2,800, issue penalties for delays in settling required taxes, and most significantly, settle tax matters outside of court.

18. (SBU) Comment: Working closely with the Ministry of Finance, a USAID project helped to prepare first an analysis of the tax system in Jordan and then the comprehensive tax reform proposal. USAID

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also helped draft the new tax code, assisted the Finance Ministry's macro-fiscal unit in estimating the impact of draft legislation, and supported the Ministry's public outreach efforts. The end result represents an unquestionable step in the right direction. The laws alone, however, will not solve all of Jordan's problems. Better enforcement is needed to pursue evaders, and greater coordination is required between the Tax Department and the government entities crucial to taxation. Collaboration is a must because although the tax laws increased penalties on evaders, the crime is not considered a felony, and with a maximum penalty of \$700 and one year in jail, the deterrent is largely considered insufficient.

19. (SBU) Comment continued: The new laws, intended to be revenue neutral in the first year, are also likely to negatively affect tax revenues in 2010 because of reduced income tax revenue (more than 98% of public and private sector employees earn less than \$34,000 a year) and because of poor corporate performance in 2009 as a result of the global financial crisis. To compensate for this income loss, the government will most likely reinstate general sales taxes, waived in 2008, on items such as cement and iron. To generate income, the GOJ has already added two items to the special tax schedule: oil derivatives and airline tickets for travel outside of Jordan. Deputy Governor of the Central Bank Kholoud Saqqaf further speculated that with these taxes and increases in other sales taxes, "Jordan would be alright" on the tax front because individuals and companies can avoid income tax, but consumers have no choice but to pay sales tax.

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